

MAY 22 1986

99TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
99-472

VA HOME LOAN GUARANTEE

FEBRUARY 20, 1986.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. MONTGOMERY, from the Committee on Veterans' Affairs,
submitted the following

REPORT

[To accompany H.R. 4130]

[Including cost estimate of the Congressional Budget Office]

The Committee on Veterans' Affairs, to whom was referred the bill (H.R. 4130) to establish, for the purpose of implementing any order issued by the President for fiscal year 1986 under any law providing for sequestration of new loan guarantee commitments, a guaranteed loan limitation amount applicable to chapter 37 of title 38, United States Code, for fiscal year 1986, having considered the same, report favorably thereon with an amendment by voice vote, and recommend that the bill as amended do pass.

The amendment (stated in terms of the page and line numbers of the introduced bill) is as follows:

Page 2, line 2, strike out "\$17,600,000,000" and insert in lieu thereof "\$18,200,000,000".

INTRODUCTION

On February 1, 1986, the President issued a sequestration order pursuant to Public Law 99-177, the Balanced Budget and Emergency Deficit Control Act of 1985, which incorporated an \$11.5 billion ceiling on the VA Guaranteed Home Loan Program.

On February 5, 1986, Hon. Richard Shelby, Chairman of the Subcommittee on Housing and Memorial Affairs, introduced H.R. 4130, to raise the ceiling to \$17.6 billion. The Committee subsequently received reports from both the VA and CBO indicating that the figure adopted in the Presidential sequestration order was greatly understated. The Congressional Budget Office now estimates that VA loan originations will be "between \$16 and \$17 billion" and the Veterans Administration estimates originations of \$19.2 billion.

71-006 O

COMPLETED
ORIGINAL

BEST COPY AVAILABLE

On February 19, by voice vote, the Committee ordered H.R. 4130 reported, as amended, to the House.

BACKGROUND

Operation of the Veterans' Administration Loan Guaranty Revolving Fund.—The VA's Loan Guaranty Revolving Fund (the Fund), established by 38 U.S.C. 1824, is a business-type revolving fund which supports the housing loan guaranty activities of the Veterans' Administration. The Veterans' Administration guarantees home loans made by private lending institutions. The guaranty is equal to 60% of the value of the loan up to a maximum of \$27,500. The VA does not incur a financial obligation from a Government accounting perspective at the time that a loan is guaranteed. It merely promises to pay in accordance with the terms of the guaranty, as authorized by chapter 37 of title 38, in the event of an incurable default by the veteran purchaser. When an incurable default occurs and the mortgage is foreclosed by the lender (or a legally equivalent event occurs), the VA is legally obligated to pay the claim of the lender subject to certain financial limitations set out at 38 U.S.C. 1816. In order to cut the potential loss on the lender's claim, the VA will often purchase the foreclosed property from the lender and attempt to resell the property.

The amount of the lender's claim and other expenses incurred by the VA in managing and disposing of the property are legal obligations of the Government. At the time that such obligations are paid, they are recorded as outlays of the United States and the Fund. The Fund generates receipts through a variety of mechanisms, including money received from the sale of defaulted properties which the VA has acquired, and from loans which the VA makes to finance the sale of such properties. In addition, at the time that the VA guarantees a loan, a 1% funding fee is collected at settlement and deposited in the fund. See 38 U.S.C. 1829. The Budget of the United States Government for Fiscal Year 1986 (the FY 1986 Budget) projected that the VA would collect \$152.6 million as a result of the fee; loan guaranty commitments were projected at \$15.429 billion. See Budget of the United States Government FY 1986, Appendix p. I-X15.

For at least the past five years, the Government has been attempting to budget for outlays which result from loan guaranty commitments. As the Government's exposure in the form of loan guaranty commitments grows, the chance of default tends to increase, so that eventually outlays may occur. In some cases, such as the Government's FHA loan program, the President proposes and the Congress enacts a ceiling on the total amount of loan principal which can be guaranteed. In the case of the VA, an estimate of the principal amount is made, but no ceiling has ever been proposed or enacted. The reason is that the provisions of title 38 entitle an eligible veteran to the home loan guaranty benefit.

Effect of Public Law 99-177.—The sequestration provision of Public Law 99-177, the Balanced Budget and Emergency Deficit Control Act of 1985 (commonly known as "Gramm-Rudman-Hollings"), was triggered for fiscal year 1986 when the Congressional Budget Office and the Office of Management and Budget (OMB)

issued a joint report to the Comptroller General on January 15, 1986, see 51 Fed. Reg. 1919, pursuant to the requirements of section 251 of the Act. In that report, the Directors of the two Offices specified the amounts and percentages by which spending in the various affected Federal budget accounts should be reduced to meet the deficit-reduction target set out in the Act. Reductions in non-defense programs "shall be made in *outlays* under other accounts of the Federal Government". Sec. 251(a)(3)(B). (Emphasis supplied.) The law requires the Directors to calculate sequestrations and reductions for non-defense programs "so as to reduce new budget authority, new loan guarantee commitments, new direct loan obligations, obligation limitations, and spending authority as defined in section 401(c)(2) of the Congressional Budget Act of 1974 *to the extent necessary to achieve any remaining required outlay reductions.*" Sec. 251(a)(3)(F)(iv)(I). (Emphasis supplied.)

Pursuant to the Comptroller General's report for fiscal year 1986, see 51 Fed. Reg. 2813, the President issued the required initial sequestration order on February 1, 1986. See 51 Fed. Reg. 4291. In large measure, the President's order incorporated the estimates prepared by CBO and OMB. CBO estimated that VA loan guaranty commitments would total \$11.9 billion, while outlays would be a negative \$122 million. Negative outlays are the result of the Fund collecting receipts in excess of obligations incurred. OMB's estimate was similar—\$12.1 billion in loan guaranty commitments and negative outlays of \$127 million. The average of the two loan guaranty commitment estimates was determined, and then mathematically reduced by the overall 4.3% reduction applied to other types of budgetary resources. The amount of new loan guarantee commitments which VA is authorized to make in fiscal year 1986 was reduced from the average of the CBO and the OMB estimate by \$515 million. Because VA's authority to guarantee loans is reduced, the amount of offsetting receipts derived from the 1% funding fee is also reduced; the net effect is an increase in outlays in FY 1986 as a result of the Presidential sequestration order, although savings in future years may occur as a result of the lower value of loans guaranteed.

On January 29, the Chairman of the Subcommittee requested the Directors of CBO and OMB and the Administrator of Veterans' Affairs to furnish the Committee with current estimates of VA home loan originations which took into account the most recent data concerning requests for VA loan guarantees. According to the replies received from VA and CBO, the estimates included in the January 15 Federal Register notice did not take into account low home-mortgage interest rates which are prevalent in today's market.

In its reply to the Committee, CBO revised its previous estimate of VA loan originations. CBO now projects that VA could guarantee loans the principal amount of which would be between \$16 and \$17 billion. CBO noted, however, "that estimates of home loan activity contain a high degree of uncertainty. A wide variety of factors, including but not limited to mortgage interest rates and general economic activity, could cause the loan volume to be significantly different from these estimates."

The VA reply was similar. The Acting Administrator stated: "Our current thinking is that VA would guarantee approximately

270,000 loans amounting to \$18.2 billion during FY 1986, without the limitation imposed by Pub. L. 99-177." The estimate used by OMB in the January 15 Federal Register notice was provided by the VA in mid-1985 in conjunction with the FY 1987 budget process, and did not reflect the decline in home mortgage interest rates since that time.

DISCUSSION OF THE BILL

The intent of Gramm-Rudman-Hollings is deficit reduction. Although there is an increase in the deficit for the current fiscal year if an arbitrary ceiling on the VA Home Loan Guaranty Program is set, the Committee nevertheless believes that if loan activity must be diminished by 4.3%, then the reduction should be applied to an accurate ceiling.

H.R. 4130 would correct the estimate adopted in the Presidential sequestration order. CBO now estimates that VA loan originations will be "between \$16 and \$17 billion" instead of the \$11.9 billion originally estimated, and the VA estimates originations will be \$18.2 billion instead of \$12.1 billion.

Since CBO has admitted that their estimates contain a high degree of uncertainty, the Committee bill incorporates the \$18.2 billion figure supplied by the Veterans Administration. Guaranteed home loan activity to date for FY 1986, as of December 31, 1985, has been approximately 62,500 loans totalling \$4.2 billion, and the VA currently estimates guaranty activity of approximately 270,000 loans in the amount of \$18.2 billion without the limitation imposed by the Balanced Budget and Emergency Deficit Control Act of 1985.

The effect of this legislation is not to circumvent Gramm-Rudman-Hollings, but to assure its proper application. Therefore, the bill requires a 4.3% reduction home loan guaranty activity from a corrected baseline.

OVERSIGHT FINDINGS

No oversight hearings were held on the reported bill by the Committee on Veterans' Affairs.

No oversight findings have been submitted to the committee by the Committee on Government Operations.

BUDGET STATEMENT

The following letter was received from the Congressional Budget Office concerning the cost of H.R. 4130:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, February 14, 1986.

Hon. G.V. MONTGOMERY,
Chairman, Committee on Veterans' Affairs,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: In response to your request, CBO has prepared the attached cost estimate for H.R. 4130, as introduced in the House of Representatives, February 5, 1986.

If you wish further details on this estimate, we will be pleased to provide them.

With best wishes,
Sincerely,

JAMES BLUM
(For Rudolph G. Penner).

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

1. Bill number: H.R. 4130.
2. Bill title: None.
3. Bill status: As introduced in the House of Representatives, February 5, 1986.
4. Bill purpose: For the purpose of implementing the order issued by the President for fiscal year 1986 under Public Law 99-177, the Balanced Budget and Emergency Deficit Control Act of 1985, this bill would increase the level of new loan guaranty commitments under chapter 37 of title 38, U.S.C., to an amount equal to \$17.6 million reduced by 4.3 percent.
5. Estimated cost to the Federal Government:

[By fiscal years, in millions of dollars]

	1986	1987	1988	1989	1990	1991
Budget authority	0	-2	54	19	0	27
Outlays	-51	49	54	19	21	12

The cost of this bill would fall in budget function 700.

Basis of estimate: The limitation on new veterans' loan guaranty commitments in the President's order under Public Law 99-177 is approximately \$11.5 billion. This bill would raise that limitation to more than \$16.8 billion, which would exceed the CBO estimate of the loan activity that would occur in the absence of a limitation.

In 1986 it is estimated that the higher loan limitation would result in an increase in loan origination fees of around \$51 million. Outlays in 1986 would fall by an equivalent amount. In 1987 and later years, however, outlays from the Loan Guaranty Revolving Fund would be expected to increase, as the higher volume of 1986 loans resulted in increased default costs.

This estimate was prepared using a computer model that interrelates the various obligation and receipt activities of the Loan Guaranty Revolving Fund based on their historical relationships and projects these factors using past trends and expectations of future economic activity.

6. Estimate cost to State and local government: The Congressional Budget Office has determined that the budgets of state and local governments would not be directly affected by enactment of this bill.

7. Estimate comparison: None.

8. Previous CBO estimate: None.

9. Estimate prepared by: K.W. Shepherd.

10. Estimate approved by: James L. Blum, Assistant Director, for Budget Analysis.

COST

The committee agrees with the Congressional Budget Office cost estimate of the reported bill.

INFLATIONARY IMPACT STATEMENT

The reported bill will have no inflationary impact.

REPORTS

On February 5, 1986, the Committee received revised estimates on VA guaranteed home loan activity as follows:

VETERANS' ADMINISTRATION,
OFFICE OF THE ADMINISTRATOR OF VETERANS' AFFAIRS,
Washington, DC, February 5, 1986.

Hon. RICHARD SHELBY,
*Chairman, Subcommittee on Housing and Memorial Affairs,
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: In response to your letter of January 29, 1986, following is an explanation as to how VA arrived at its estimate of loan originations for FY 1986.

The initial estimates of workload are prepared within the Department of Veterans Benefits as part of the internal budget process. Specifically, the Loan Guaranty Service has principal responsibility for developing these projected workloads. Multi-year budget projections encompass a wide range of considerations such as veteran population statistics and long range economic forecasts. However, short range projections are more influenced by current trends, particularly interest rates, appraisal requests, and new housing starts. These items are valid indicators of future loan activity in the near term.

Mortgage interest rates clearly have the most weight in estimating the level of loan activity. The latest estimate for FY 1986 was made this past summer in conjunction with the FY 1987 budget process. At that time the maximum interest rate for home loans was 11½ percent. Based on all the information available to us at that time, our estimate was for a modest increase in loan volume in FY 1986 over the FY 1985 level of \$11.5 billion. In mid November 1985 mortgage interest rates began dropping significantly. On December 13, 1985 VA lowered its maximum home loan rate to 10½ percent, the lowest level in 6 years. VA clearly did not expect this sharp decrease in interest rates at the time the FY 1986 estimate was made. Activity to date for FY 1986, as of December 31, 1985, has been approximately 62,500 loans totalling \$4.2 billion. Our current thinking is that VA would guarantee approximately 270,000 loans amounting to \$18.2 billion during FY 1986, without the limitation imposed by Pub. L. 99-177, the Balanced Budget and Emergency Deficit Control Act of 1985.

I hope the information we have provided will be useful to you.

Sincerely,

EVERETT ALVAREZ, Jr.,
Acting Administrator.

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, February 5, 1986.

Hon. RICHARD SHELBY,
Chairman, Subcommittee on Housing and Memorial Affairs, Committee on Veterans' Affairs, House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: This is in response to your letter of January 29, 1986, inquiring into the CBO estimate of VA home loan originations in fiscal year 1986. An average of the CBO estimate and an estimate prepared by the VA constituted the base upon which the Gramm-Rudman sequester was calculated.¹

The CBO estimate of 1986 loan originations was based on preliminary actual data for fiscal year 1985 provided by the VA. The preliminary data indicated that loan volume had remained fairly steady during 1985 at approximately 15,000 new loans guaranteed per month. Based on these data, CBO estimated a small increase in new loan originations and a slight decrease in refinancing loans for 1986. The VA had provided a very similar estimate for inclusion in the President's FY 1987 budget. An average of the CBO and VA estimate was used for the sequester order.

This week we received "final" actual data for fiscal year 1985. These data show loan volumes rising in July and averaging almost 1,200 more loans per month than had been recorded in the preliminary data. In addition, we have received actual data for the first quarter of FY 1986, which indicate a continued increase in loan activity. In light of this new information, it now appears that the CBO estimate of unrestrained loan activity in 1986 may be too low. We would currently estimate such loan activity at approximately 21,000 loans per month, which would result in a total loan volume of between \$16 and \$17 billion. This compares with our earlier estimate of a 1986 loan volume of \$11.9 billion. It should be noted, however, that estimates of home loan activity contain a high degree of uncertainty. A wide variety of factors, including but not limited to mortgage interest rates and general economic activity, could cause the loan volume to be significantly different from these estimates.

With best wishes,
Sincerely,

RUDOLPH G. PENNER, *Director.*

¹ The sequester was applied only to new guaranteed loans originated by the VA. Certain direct loans held by the agency that are sold with a guaranty are not subject to sequester, even though they are considered new loan guarantees and included in the total amount of guaranty commitments made by the agency. This discussion pertains only to sequesterable new loan originations.